

CAPITAL PROJECTS AND BOND OVERSIGHT COMMITTEE

Minutes

December 13, 2005

The Capital Projects and Bond Oversight Committee met on Tuesday, December 13, 2005, at 10:00 AM, in Room 129 of the Capitol Annex. Representative Mike Denham, Chair, called the meeting to order, and the secretary called the roll.

Present were:

Members: Senator Elizabeth Tori, Co-Chair; Representative Mike Denham, Co-Chair; Senators Tom Buford and Dan Seum; and Representatives Paul Marcotte and Jim Wayne.

Guests testifying before the Committee: Larry Owsley, University of Louisville; Ken Clevidence and Sergio Melgar, University of Kentucky; John Hicks, Governor's Office for Policy and Management; Jim Abbott and Steven Biven, Finance and Administration Cabinet; Sandy Williams, Kentucky Infrastructure Authority; Terri Fugate, Office of Financial Management; and Bill Davis, Ogden Newell & Welch PLLC.

LRC Staff: Mary Lynn Collins, Pat Ingram, Nancy Osborne, Kristi Culpepper, Bart Hardin, and Shawn Bowen.

Representative Marcotte made a motion to approve the minutes of the November 11, 2005 meeting. The motion was seconded by Senator Seum and approved by unanimous voice vote.

Representative Denham called on Ms. Mary Lynn Collins, Committee Staff Administrator, to review correspondence items. Ms. Collins said members' folders included five items of correspondence: a follow-up report from the Department for Facilities and Support Services, Finance and Administration Cabinet, listing state contracts relating to the proposed Louisville Arena project; correspondence from the Department of Commercialization and Innovation reporting one grant exceeding \$400,000 from the High Tech Investment/Construction Pool; correspondence submitted by the University of Louisville and the University of Kentucky reporting the purchase of unbudgeted scientific research/medical equipment; and the Kentucky Lottery Corporation's monthly financial report for October 2005.

Ms. Collins said also included in Committee folders was a staff update on various capital projects and a notice by the Finance Cabinet that they plan to use the Construction

Management-at-Risk project delivery method for construction of the Northern Kentucky Regional Special Events Center.

Representative Denham asked Mr. Abbott if he would make a presentation to the Committee regarding the proposed Louisville Arena project once all the contracts are finalized. Mr. Abbott responded that he would be glad to update the Committee on the project at a future date.

Senator Seum introduced a special guest, Ms. Katia Kolerova, from Moscow, Russia. He said Ms. Kolerova is an intern visiting the United States for the next six months.

Representative Denham called on Larry Owsley, Vice President for Finance and Administration, University of Louisville (U of L), to discuss plans by the University to design a basketball practice facility. Mr. Owsley said U of L received authorization in the current budget for a \$9.6 million project to expand Cardinal Arena. The purpose of the expansion is to meet gender equity requirements under NCAA policies and Title IX requirements.

Mr. Owsley said as the University began planning the expansion, they encountered construction and cost issues relating to high voltage power lines along an adjacent street. The University has now determined that it would be cost prohibitive and unsafe to continue the expansion project, and a better option would be to build a freestanding facility on Floyd Street on vacant land. The University plans to seek authorization for the facility (\$16 million) during the 2006 Session and the project is included in the 2006-2008 Capital Budget Recommendation by the Council on Postsecondary Education. Mr. Owsley said the University would like to move forward with the design of the facility using \$575,000 in private funds.

In response to a question from Representative Denham, Mr. Owsley said the \$575,000 to be used for design is all private funds, and the University has the funds in hand now.

Representative Wayne made a motion to approve the unbudgeted design project for U of L. The motion was seconded by Senator Tori and passed by unanimous roll call vote.

Representative Denham next called on Ken Clevidence, Associate Vice President for Fiscal Affairs, University of Kentucky, to report two new leases. Mr. Clevidence introduced Sergio Melgar, Vice President and Chief Financial Officer, UK Healthcare Enterprises. Mr. Clevidence reported that the University has established a 19-month lease (PR-8287, UK Department of Computational Sciences) with e-Cavern, Inc. in Louisville, Kentucky. The lease, mandated by federal legislation and paid for by the U.S.

Department of the Treasury, is needed to conduct research in improving the resiliency of the financial sector to recover from various disaster scenarios through the development of new, secure remote financial transaction back-up storage systems. The cost of the 19-month lease will be \$729,140, and is 100% federally funded.

Representative Wayne said the Committee may be interested in touring e-Cavern in the future. He said e-Cavern is located in his district, and extends under the Louisville Zoo, the expressway, and the Louisville International Airport.

Representative Wayne made a motion to approve the lease. The motion was seconded by Senator Tori and approved by unanimous roll call vote.

Mr. Clevidence next reported an emergency lease modification for PR-8282, UK Hospital Finance. He said the UK Healthcare Enterprise is in the process of planning new patient care facilities, and as part of this planning effort, they have found it necessary to relocate several of the University's business operations to other space off campus. The vacated space will then be renovated to accommodate UK clinical operations to be moved into the hospital complex.

Mr. Clevidence said the University currently leases 6,644 square feet at \$16.40 SF at 2347 Sterlington Road, and the lessor (Shawn Sabharwal) is willing to lease an additional 34,563 SF at the same rate. Mr. Clevidence said the University also plans to make improvements to the property at a cost of \$539,427. Those costs will be amortized over the remaining 53 months of the lease. Including the cost of the improvements, and the additional square footage, the annual cost of the lease will be \$794,182.

Mr. Melgar said UK Healthcare Enterprises has been extremely successful over the past two years, and continues to experience double digit growth rates. He said it is now vital to move any personnel that are not clinical and mission critical off the hospital site, in order to expand clinical services and provide flexibility in the new building site.

Representative Denham noted that this lease is being procured by emergency order (pursuant to KRS 56.805(3)), and, as such, no Committee action is required. However, he said he had serious concerns and reservations about this lease. He asked why this lease was not competitively bid. Mr. Clevidence said that the initial space the University leased at this location, PR-8231, UK Hospital Marketing Department, was competitively bid. Mr. Melgar said there are approximately 200 staff spread over multiple locations, and this move would bring them all together. He explained that there is a significant benefit and flexibility to the organization if they can keep the groups together.

In response to a question by Representative Denham, Mr. Clevidence said when the initial lease was bid, the SF rate offered by Sabharwal, \$16.40, was somewhat higher

than some of the other offers, but those other offers would not have allowed for expansion.

Representative Denham said he appreciated what the University was trying to do. He said he still had problems with a lease of this size not being bid.

In response to a question to Representative Wayne, Mr. Clevidence explained that the original lease at Sterlington Road, PR-8231, UK Hospital Marketing Department, was competitively bid (2001). The lease being discussed today, PR-8282, UK Hospital Finance, was not competitively bid, but was created in June 2005 by amending the original Sterlington Road lease. He noted that this was the second non-competitively bid lease to be placed in the same building within the period of a few months.

Representative Wayne asked why this lease is being submitted as an emergency since it should take no more than eight weeks to bid it competitively. Mr. Clevidence said it is considered an emergency based on the size of the scope of the lease, and because it does not have a line-item authority from the General Assembly.

Representative Wayne said it appears that UK's management is not very clear in its long-term planning when it submits two non-competitive leases within a few months apart, and this kind of action raises a lot of questions. Mr. Melgar said the University has had double digit growth rates for the last two years. He said they originally thought adding one floor to the lease would be sufficient for the University's needs, at least for the next 12-18 months. As they moved into the space and the volume continued to grow, it became very clear that they were going to have to expand much more than what they had planned six months before. He said they have added 500 employees in the last 24 months, and are looking to add an additional 200 employees before the end of June 2006.

Representative Wayne said it seems that the University is indicating that because it is growing so fast, it needs to rush through the lease procurement process. He said the Committee is cautioning the University that it should not rush through the process, and should allow the time needed to conduct a competitive bid process; by doing so, the University may get a better deal, or at least, it may allow the University to renegotiate who should pay the fit-up costs for this lease.

Representative Wayne asked why the University is paying all of the fit-up costs for this lease, especially on the floor that is currently unfinished "shell" space. Mr. Melgar said the landlord is not paying the cost of the renovations because the renovations will benefit the University.

Representative Wayne asked if the landlord or any his family members have made any donations to the University within the last five years. Mr. Clevidence said he did not

have any information about whether or not the landlord has made donations to the University.

In response to a question by Mr. Clevidence, Representative Wayne said that when a landlord has a no-bid lease that costs over \$3 million annually, when a lease is expanded twice without any bids, and the University spends \$539,427 to make improvements that should be paid for by the landlord, it is an unusual situation, and it raises questions. He said if the landlord has any linkages to the University, the Committee needs to know. Mr. Clevidence said he would get the information for the Committee.

Senator Buford said because of the construction of the new Bed Tower, he understood the situation the University faces. He said in the process of constructing the new Bed Tower, this may just be the first of inconveniences the University has to go through. He said considering crowded campus conditions, he did not see that the University had much of an option except to move forward in this manner.

Mr. Melgar said the University's plans in the future are to have significant Hospital expansion, and they will likely go to this site again. He said one of the benefits of the Sterlington Road location is that it is a multiple building site. As leases expire and space becomes available on that site, it would be in the University's best interest to aggregate its personnel there as much as possible.

Representative Denham said the Committee understands why the University wants to consolidate its operations; however, he said no bid contracts of this nature have in the past created a lot of discomfort for the legislature, the University, and for others.

Representative Denham said no action needs to be taken for this project since it is an emergency project, but he asked staff to prepare a letter to the Council on Postsecondary Education asking it to consider the appropriateness of this lease in regard to the fact that it was not bid and that it calls for over \$500,000 in improvements to the privately-owned property. He said the University can run into serious problems by not bidding these contracts, and while the Committee's intent is to work with the University, and not hold it up, this contract is one for concern. He said the University should consider bidding these contracts in the future.

Representative Wayne said the Committee is just doing its job in terms of providing that accountability.

Representative Denham asked John Hicks, Deputy State Budget Director, Governor's Office for Policy and Management, and Jim Abbott, Commissioner for the Department for Facilities and Support Services, Finance and Administration Cabinet, to present the Finance Cabinet's monthly report to the Committee.

Mr. Hicks first reported that it has authorized an emergency capital project to replace the heating, ventilation, and air-conditioning system in the Denham Building at the Maysville Community and Technical College. He said in 2004 the Kentucky Community and Technical College System (KCTCS) initiated a project under \$400,000 to extend to the Denham Building the geothermal HVAC system that was installed in the Administration/Academic Building as part of the Emergency Structural Repair and Mold Abatement project reviewed by the Committee in 2001 and 2002. However, the project bore the unanticipated expense of a mold abatement (\$27,000) that was necessitated by leaking HVAC piping. The project, now estimated at \$482,000, has exceeded the statutory threshold of \$400,000. (All projects in excess of \$400,000 are required to be approved by the General Assembly unless 50% of the costs will be funded from federal or private sources or the project relates to an emergency situation.)

Mr. Hicks said the project will be funded from KCTCS's own restricted funds, and Secretary Rudolph has approved this project as an emergency because of the existing conditions of the HVAC system and the potential problems associated with mold growth.

Representative Denham said emergency projects must be reported to the Committee within 30 days, and no further Committee action is required.

Mr. Hicks next reported an unbudgeted federally funded project for Kentucky State University. He said the University plans to construct a Land Grant Farm Facility at the University's cooperative extension research farm in Franklin County. The project includes a 8,900 SF facility that will include a welcome center, a pavilion, and a 2,400 SF Apiculture Building for the University's beekeeping program. The proposed project scope is \$1,578,700, and the project will be totally funded by the U.S. Department of Agriculture. The federal agency will pay operating and maintenance costs.

Senator Tori made a motion to approve the Land Grant Farm Facility project for Kentucky State University. The motion was seconded by Senator Buford and passed by unanimous roll call vote.

Lastly, Mr. Hicks reported an unbudgeted purchase of scientific research equipment by Northern Kentucky University. The University has purchased an Atomic Force Microscope at a cost of \$212,470, that will be paid for with federal funds. The microscope will help support research activities in the departments of Biological Sciences, Chemistry, and Physics and Geology. Representative Denham said this item did not require any Committee action.

Mr. Abbott and Steve Biven, Director, Division of Real Properties, presented one lease report for PR-3882, Department of Revenue and the Commonwealth Office of Technology (COT) in Franklin County. Mr. Biven said COT is currently working with the Department of Revenue on a tax modernization project, and requires space within

close proximity of the Department of Revenue. He said the Revenue Cabinet is modifying 3,422 SF of warehouse space it currently leases to accommodate COT's relocation to this facility. The cost of the renovations will be \$82,749, and will be amortized over the remaining lease term through June 30, 2010.

Senator Buford made a motion to approve the lease modification report. The motion was seconded by Senator Tori and approved by unanimous roll call vote.

The next report was presented by Sandy Williams, Kentucky Infrastructure Authority (KIA). Ms. Williams reported four new KIA loan requests. The first request was a Fund A (Federally Assisted Wastewater Revolving Loan Fund) loan for the City of Cynthiana in Harrison County. The proceeds of the loan, \$5,804,150, will be used to construct a new wastewater treatment plant.

Senator Buford made a motion to approve the Fund A loan for the City of Cynthiana. The motion was seconded by Representative Wayne and passed by unanimous roll call vote.

Ms. Williams next reported a Fund A loan in the amount of \$812,000, and a Fund B loan (Infrastructure Revolving Loan Fund) in the amount of \$1,446,500, for the Western Mason Sanitation District in Mason County. The proceeds from the Fund A loan will be used to construct a new sewer collection system, and the proceeds from the Fund B loan will be used to address cost elements that were over the project budget when it was bid.

Representative Denham said this project was started in 1996, and is critical to the development of Mason and Bracken Counties.

Senator Buford made a motion to approve the Fund A and B loans for the Western Mason Sanitation District. The motion was seconded by Representative Wayne and passed by unanimous roll call vote.

Ms. Williams reported that the City of Hardinsburg, Breckinridge County, is requesting a \$4,000,000 Fund F loan (Federally Assisted Drinking Water Revolving Loan Fund). The proceeds of the loan will be used to construct a water treatment plant.

Senator Tori made a motion to approve the Fund F loan. The motion was seconded by Senator Buford and passed by unanimous roll call vote.

Ms. Williams said also included in members' folders was a report from KIA regarding 55 line-item Coal/Tobacco Development Grants approved in the 2004-06 budget.

The next report was provided by Ms. Terri Fugate, Financial Analyst, Office of Financial Management. Ms. Fugate presented one new bond issue report: Kentucky Economic Development Finance Authority (KEDFA) Variable Rate Demand Hospital Facilities Revenue Bonds, Series 2005B, (Baptist Healthcare System Obligated Group), Periodic Auction Reset Securities (PARS). The proceeds from this issue, \$61,750,000, will be used to finance the construction of facilities at five hospitals and Baptist Healthcare System Support Services at the St. Matthews, Lexington, Paducah, Corbin and LaGrange locations.

Ms. Fugate said the sale of these bonds is contingent upon the issue's approval at the December 16 KEDFA meeting and the December 19 State Property and Buildings Commission meeting. Normally, the issue would not be brought to the Committee prior to these approvals, and is only being done so in this case because of the decision by the Committee to move its December 20 meeting date to December 13.

Senator Seum asked if the Baptist Hospital of Louisville is a private entity. Mr. Bill Davis, Bond Counsel, Ogden Newell & Welch, responded that Baptist Hospital is owned by Baptist Healthcare System, Inc., which is a Kentucky non-profit corporation. Mr. Davis said in order to issue tax-exempt bonds, the non-profit corporation must use KEDFA as the conduit issuer for these bonds. He said the bonds are payable solely from payments made by Baptist Healthcare to the bond trustee, and the state has no liability for repayment of the bonds. He said in order for Baptist Healthcare to avail itself to tax-exempt interest, it has to use either a city, county, or KEDFA to issue bonds. He said there are five hospitals involved, and to eliminate the need for five separate issues, bond counsel asked KEDFA to issue the bonds.

Senator Buford made a motion to approve the KEDFA bond issue contingent upon the issue's approval at the December 16 KEDFA meeting and the December 19 State Property and Buildings Commission meeting. The motion was seconded by Representative Marcotte and passed by unanimous roll call vote.

Ms. Fugate presented two follow-up reports for previously approved bond issues: Kentucky Asset/Liability Commission Project Notes, 2005 General Fund Second Series A-1 and A-2 and 2005 Taxable General Fund Second Series C-1, \$750,000,000; and Kentucky Asset/Liability Commission University of Kentucky General Receipts Project Notes, 2005 Series A, dated November 8, 2005, \$107,540,000. Representative Denham said these follow-up reports were for previously approved bond issues, and no further action was required.

Ms. Fugate presented one new school bond issue with School Facilities Construction Commission (SFCC) debt service participation for the Corbin Independent School District in Whitley County.

Senator Tori said schools must maintain 2% of their budget for a reserve fund. She asked why the Corbin Independent School District is not using some its reserve fund for this \$368,000 renovation project. Ms. Fugate responded that she did not know, but she would find out and let Senator Tori know.

Senator Buford made a motion to approve the school bond issue. The motion was seconded by Representative Marcotte and passed by unanimous roll call vote.

Ms. Collins said there were six locally-funded school bond issues submitted to the Committee for review this month: Kentucky Interlocal School Transportation Association (KISTA); Allen County; Johnson County; Montgomery County; Pike County; and Russell County. She said all disclosure information has been filed, and no further action on the bond issues was required.

Also included in members' folders was the debt issuance calendar. No action was required for this report.

With there being no further business, the meeting adjourned at 10:50 a.m.